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Supreme Court of the United States

OCTOBER TERM, 1965

No. 463

IN THE MATTER
of
J. E. SCHECTER CORPORATION,
Petitioner,
and
CARRIER CORPORATION, AMERICAN RADIATOR & STANDARD SANITARY CORPORATION, SARCO COMPANY, INC. and SARCOTHERM CONTROLS, INC.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

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Opinions Below

The opinion and order of the Referee in Bankruptcy appear in the Appendix at pages 31a through 39a. The opinion of the United States District Court for the Eastern District of New York which upheld the decision of the Referee in part, but remanded the matter to him for further proceedings, is reported at 234 F. Supp. 474. The opinion of the Court of Appeals for the Second Circuit, which reversed the decision of the District Court and dis-

missed the cross-appeal of the petitioner, is reported at 347 F. 2d 153 and also appears with the judgment of the Court of Appeals at pages 28 through 34 of the petition.

Jurisdiction

The judgment of the Court of Appeals was entered on May 21, 1965. The petition for certiorari was filed on August 17, 1965. Jurisdiction of this Court is invoked under 28 U. S. C. § 1254 (1) and Section 24c of the Bankruptcy Act, 11 U. S. C. § 47c.

Statutes Involved

Respondents find no fault with the citation by petitioner of the relevant New Jersey statutes, except that the captions are not completely accurate. Title 2A of the New Jersey statutes is captioned: "Administration of Civil and Criminal Justice." Subtitle 6 thereunder is captioned "Specific Civil Actions," and Subtitle 10 is captioned "Crimes." Lest undue emphasis be placed on captions and cross-references, the Court's attention is directed to the Preamble to Title 2A, paragraph 7 which provides:

> "The classification and arrangement of the several sections of said Title 2A have been made for the purpose of convenience, reference and orderly arrangement, and therefore no implication or presumption of a legislative construction is to be drawn therefrom."

and to paragraph 8 which states:

> "In the construction of the said Title 2A . . . no outline or analysis of the contents of said title or of any subtitle . . . no cross-reference or cross-reference note and no headnote or source note to any section of the said Title 2A shall be deemed to be a part of the said Title."

On the trust fund issue, no federal statute is involved, the Bankruptcy Court merely being the forum for determining rights to a fund in the Court's actual or constructive possession. It is undisputed that local law is crucial on that issue.

The Bankruptcy Act is involved only by petitioner's "Argument" on counsel fees, but not by mention in "Questions Presented For Review" or the "Statement of the Case". Petitioner contends that the Bankruptcy Act makes no provision for counsel fees in this case. Respondents contend that insofar as the Bankruptcy Act vests the Bankruptcy Court with equity powers, such power includes the traditional power to allow counsel fees when a fund is created for the benefit of others.

Chapter 2 of the Bankruptcy Act (11 U. S. C. § 11) provides:

> "CREATION OF COURTS OF BANKRUPTCY AND THEIR JURISDICTION. (a) The Courts of . . . bankruptcy . . . are hereby invested . . . with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this act . . ."

The New York Lien Law, Section 70 *et seq.* was involved in the courts below and appears in part in the appendix (9a), but for present purposes need not be repeated here.

Questions Presented for Review

Should this Court exercise its sound judicial discretion and grant certiorari when:

(a) The Court of Appeals has not decided an important New Jersey question in conflict with applicable New Jersey law, but in fact is entirely in accord with it; and when

(b) No federal issue is involved, although petitioner raises the *Erie* v. *Tompkins* doctrine so as to fall within this

Court's appellate jurisdiction, notwithstanding that the Court of Appeals clearly applied local law; and when

(c) The Court of Appeals left unanswered alternative grounds for relief under New York and New Jersey statutes by granting relief under New Jersey decisional law and New Jersey as well as general principles of equity and justice; and when

(d) The petitioner, on the question of counsel fees payable out of the fund, is not an aggrieved party and therefore has no standing to appeal, and when, in any event, the decision of the Court of Appeals on the issue of compensation is in harmony with decisions of this Court and the New Jersey courts, and not in conflict with any cited by the petitioner.

Statement of the Case

The facts appear in the opinion of the District Court in detail and in the opinion of the Court of Appeals to the extent necessary to frame the legal questions involved. Respondents cannot concur with petitioner's presentation of the case.

In January, 1961, William L. Crow Construction Company, a New York corporation, hereafter called Crow, general contractor in the improvement of real property owned by Princeton University, located in Princeton, New Jersey, and known as the "Engineering Quadrangle", entered into a subcontract with the petitioner, J. E. Schecter Corporation, hereafter called Schecter or the debtor, to provide all labor and materials for the plumbing, heating and air-conditioning work. The sub-contract provided that "All matters relating to the validity, performance, interpretation or construction of the agreement or the breach thereof shall be governed by the Law of the State of New York" (13a).

In September, 1962, Schecter wrote to Crow, setting forth the names of forty-one subcontractors and materialmen who had performed work for and/or supplied materials to Schecter for the Princeton job, and to whom Schecter was indebted, and requested Crow to pay the said claimants from the balance due Schecter a sum on account equal to 50% of the respective claims, but said sums were never paid (16a).

On November 27, 1962, Schecter filed a petition under Chapter XI of the Bankruptcy Act and an order was entered authorizing it to continue in possession of its assets, to continue in business, staying all creditors from proceeding with their claims, and referring the case to Referee in Bankruptcy, William J. Rudin.

In July, 1963, one of the unpaid subcontractors, Johnson Service Company, moved before the Referee for an order permitting it to prosecute an action against the debtor on behalf of itself and others similarly situated for an accounting of the trust funds derived from the Princeton project, but Johnson did not proceed further with the motion (27a-30a). Instead, Schecter filed a petition for an order compromising Schecter's claim against Crow for $165,000, compromising the claims of six creditors, including Johnson Service Company, against the fund for approximately 30% of their claims, with no mention of the fact that there were thirty-five other claimants and providing that the balance be paid to Schecter and deposited in a depositary designated by the Court (13a). The order was signed by Referee Rudin (11a), and the terms were thereupon carried out, with a balance of $92,816.67 being paid over to Schecter and being held in a special account in the debtor's name. No notice of this proceeding was given to the thirty-five other creditors of the debtor remaining from the Princeton job.

In December, 1963, the four respondents, on behalf of themselves and others similarly situated, petitioned the

Referee to impress a trust under the laws of New Jersey and New York on said funds in the debtor's possession and for legal fees to be paid out of said trust fund (2a-18a).

The Referee denied the petition and Judge Rayfiel upheld him on the grounds that no trust could be impressed under New York law since its Lien Law only applied to an improvement of real property located in the State of New York and that the intent of Crow and Schecter to have New York law apply must bow to the more significant contacts in New Jersey, and that the New Jersey statute was criminal in scope and provided no civil remedy for a "diversion" of funds received by a contractor for a New Jersey improvement. The District Court, however, remanded the matter to the Referee for the purpose of directing the debtor to proceed with an appropriate motion to recover the funds paid to the six creditors (47a).

The Court of Appeals reversed the District Court and impressed a trust on the funds in the debtor's possession derived from the Princeton project on equitable principles as enunciated in New Jersey cases, and allowed counsel fees out of said fund, remanding the matter to the District Court for further proceedings in accordance with the opinion. The Court of Appeals also denied the cross-appeal of the petitioner for the reason that the return of the monies paid to six creditors was mooted by the impressing of a trust.

After remand, respondents obtained an order signed by Referee Rudin dated July 29, 1965, a copy of which is set forth in the Appendix (24), which details the steps to be taken in order to implement the decision of the Court of Appeals.

The Court of Appeals, in respondents' view, did not definitely rule out the applicability of New York law or a remedy based solely on the New Jersey statute, but found it unnecessary to determine those questions as it impressed a trust on other grounds. While respondents rely primarily

on New Jersey law inasmuch as the improvement was located in New Jersey, they take the position that if the New Jersey statutory or decisional laws do not afford relief, respondents can look to New York law alternatively as a third-party beneficiary of the contractual provision which sought to apply New York law.

Respondents do not seek an allowance for counsel fees over and beyond the amounts due the unpaid claimants, but only seek it from those participants in the trust fund to be paid out of their recovery. Respondents fail to see how petitioner is affected by this part of the Court of Appeals' decision. In any event, the only question would be the power of the bankruptcy court to allow counsel fees in this type of case, and this Court has already passed affirmatively on that issue, and the cases cited by the petitioner are not in conflict with the decisions of this Court or the decision of the Court of Appeals.

Upon the undisputed facts and the applicable New Jersey law, the decision of the Court below was absolutely correct.

ARGUMENT

I

There is no basis for granting certiorari.

A. Solely State-created rights are involved and *Erie* v. *Tompkins* has no applicability.

The existence of a trust fund is strictly a question of local law and both petitioner and respondents have adopted this view. The subsidiary question of which local law to apply is not before this Court, as the Court of Appeals granted relief under New Jersey law, the choice of the petitioner and accepted by respondents as their primary basis for relief. The only question, therefore, insofar as *Erie* v. *Tompkins* (304 U. S. 64, 58 S. Ct. 817, 82 L. Ed.

1188), is concerned, is whether the Court of Appeals applied local law, and not whether they applied it correctly;

The opinion of the Court of Appeals could not be any plainer. It relied mainly on the following for its decision: (1) An expression by the highest court of New Jersey in the recent case of *Hiller & Skogland, Inc.* v. *Atlantic Creosoting Co., Inc.*, 40 N. J. 6, 20 n. 3, 190 A. 2d 380, 388, n. 3 (1963) citing with approval a decision of the Superior Court, Appellate Division of the State of New Jersey, *Samuel D. Wasserman, Inc.* v. *Klahre*, 24 N. J. Super. 143, 93 A. 2d 638, which said that if there were a violation of the private improvement statute, the Court would give "whatever civil remedy might be appropriate to the circumstances under the general principles of law and equity". (2) Holdings in several New Jersey cases wherein trusts were impressed, not directly under the statutes there involved, but under general equitable principles. *National Surety Corp.* v. *Barth*, 11 N. J. 506 (1953) and other cases cited in the opinion.

The Court of Appeals also cited a federal case in New York involving a similar statute, former Section 36a of the New York Lien Law, which was deemed to be a criminal statute, but where the Court nevertheless impressed a trust. *Wickes Boiler Co. Inc.* v. *Godfrey-Keeler, Inc.*, 2 Cir., 116 F. 2d 842, mod. 121 F. 2d 415, cert. den. 314 U. S. 686, and another case of far-reaching importance, *Filardo* v. *Foley Bros. Inc.*, 297 N. Y. 217, cert. den. 336 U. S. 281 (1948), where the New York Court of Appeals said:

> "With the beneficial results of the statute so mainfest, if plaintiff may not sue to enforce it, the benefits accorded would indeed be empty and illusory. He would find himself in the position of having been given a benefit he is unable to enjoy, a right he is helpless to enforce."

The petitioner, on the other hand, does not even mention or cite the *Hiller & Skogland* case, *supra,* which is rather astonishing when considered in the light of its contention that the Court of Appeals did not apply New Jersey law. The petitioner also makes no attempt to explain the vitally important statement made by the Appellate Court in the *Wasserman* case, as quoted in the Court of Appeals' opinion—which is the crux of this case. Thus, the petitioner has ignored the very same criteria set forth in a case it cited on pages 10-11 of its petition, *Yoder et al.* v. *Nu-Enamel Corporation,* 8 Cir., 117 F. 2d 488.

The Court of Appeals decided that New Jersey law applied and granted relief unanimously on equitable principles as enunciated by the authoritative New Jersey cases cited in its opinion, and certiorari on the grounds that *Erie* v. *Tompkins* has been ignored, should therefore be denied.

B. There are no matters of federal importance to be considered.

There is no conflict among the circuits on the issue presented, and no cases are cited in the petition to demonstrate any conflict. There is no important question of federal law which has not been, or should be settled by this Court. No issue touching the federal interest is presented. The issue is narrow and not likely to recur. The trust fund issue is strictly a matter of local law. See *Collier* on Bankruptcy, Volume 4, pages 1210-1211.

As to the power of the bankruptcy court to award counsel fees out of the fund, this matter had long ago been settled by this Court in *Trustees* v. *Greenough,* 105 U. S. 527, 533, when this Court said:

> "The rule that a party who recovers a fund for the common benefit of creditors is entitled to have his costs and expenses paid out of the fund, prevails in bankruptcy cases."

And in *Sprague* v. *Ticonic Bank*, 307 U. S. 161, 167, this Court said:

> "In any event such allowances are appropriate only in exceptional cases and for dominating reasons of justice. But here we are concerned solely with the power to entertain such a petition."

New Jersey has also accepted the doctrine of *Trustees* v. *Greenough, supra*. See *Babbitt* v. *Fidelity Trust Co.*, 72 N. J. Eq. 745, 66 A. 1076.

Any limitations that may exist on the power of the bankruptcy court to allow counsel fees are those imposed in the bankruptcy itself, and not in any controversy in equity arising out of the bankruptcy in which the bankruptcy court will follow the precedents and practice of a court of equity and allow counsel fees, referred to traditionally as costs as between solicitor and client. Even the case of *Berry* v. *Root*, 5 Cir., 148 F. 2d 945, cert. den. 326 U. S. 755, and others cited by petitioner, and which did not involve a fund before the Court, acknowledged the power to allow counsel fees under circumstances present in this case. The only reservation sometimes placed is the requirement that the benefits be accepted by the beneficiaries. However, as demonstrated heretofore, steps are under way (24) to give the other beneficiaries an opportunity to share in the fund and to accept the benefits.

In any event, the petition should not be granted solely on the question of counsel fees for the further reason that petitioner is not an aggrieved party and therefore has no standing to review the decision allowing it? Respondents do not seek any sum over and beyond the amount due the unpaid claimants for counsel fees, but merely an allowance out of the sums being paid to each creditor, so that the creditors who did not participate in this litigation are not unjustly enriched at the expense of the four claimants and their attorneys who instituted the proceeding before the

Referee, petitioned the District Court for review and then appealed to and obtained a reversal from the Court of Appeals and are now opposing certiorari before this Court. In fairness and in equity, the expenses and legal fees as determined by the District Court should be shared ratably out of the fund. The petitioner will be unaffected by this relief. The only ones affected by any allowance of counsel fees would be the thirty-five other participants in the fund against which the fees would be chargeable.

It is well-settled that an appellant cannot be heard to complain of an error which does not harm him. He must be aggrieved by the judgment or decree for which the relief is sought. It must prejudice him in his rights or adversely affect his legal interests, otherwise, he is not entitled to appeal therefrom. *Public Service Commission* v. *Brashear Freight Lines, Inc.*, 306 U. S. 204, 83 L. Ed. 608, rearg. den., 306 U. S. 669, 83 L. Ed. 1063; *Kirkpatrick* v. *Eastern Milling & Export Co.*, 135 F. 151; *Marceau* v. *Great Lakes Transit Corp.*, 2 Cir., 146 F. 2d 416; *Highway Construction Co. of Ohio* v. *City of Miami, Fla.*, 5 Cir., 126 F. 2d 777; Cyclopedia of Federal Procedure, Volume 14, 67.05, page 121.

The Court of Appeals did not decide any federal question in a way to conflict with applicable decisions of this Court, nor did it conflict with any guaranty of basic fairness secured by the Constitution or implied in the nation's laws so as to call for the exercise of this Court's power of supervision. In fact, the decision of the Court of Appeals is in furtherance of this Court's doctrines. See: *Aquilino* v. *United States of America, et al.*, 363 U. S. 509, 80 S. Ct. 1277; *Pearlman* v. *Reliance Insurance Company*, 371 U. S. 132, 135. In the latter case, this Court said:

> "Property interests in a fund not owned by a bankrupt at the time of the adjudication, whether complete or partial, legal or equitable, mortgages, liens, or simple priority of rights, are of course not a part of the

bankrupt's property and do not vest in the trustee. The Bankruptcy Act simply does not authorize a trustee to distribute other people's property among a bankrupt's creditors. So here if the surety at the time of adjudication was, as it claimed, either the outright legal or equitable owner of this fund, or had an equitable lien or prior right to it, this property interest of the surety never became a part of the bankrupt estate to be administered, liquidated and distributed to general creditors of the bankrupt."

Moreover, the Court of Appeals made it clear that the consequence of its decision would be to guarantee basic fairness and to bring about the fulfillment of the New Jersey legislative intent that funds from a real property improvement went to those who contributed to the improvement.

II

The decision below is clearly correct.

While the Supreme Court of New Jersey in *State* v. *Low*, 18 N. J. 179 (1955), and the clear language of Section 2A:102-11 of the New Jersey statutes describe the monies received as "trust funds", the New Jersey courts have not ruled squarely on the issue presented herein, i.e., whether a bankruptcy court could impress a trust under New Jersey law in favor of job claimants on funds in the possession of a debtor derived from a New Jersey improvement.

However, as noted before, clear expressions by the highest and next highest courts of the State indicate that civil relief would be afforded and formed the main basis for the decision of the Court of Appeals.

It should be noted that nothing more is sought herein than the precise application of the statute in favor of

the statutory beneficiaries and against the statutory trustee, without any complicated issue of tracing the *res*, creation of a constructive trust against funds in the hands of third parties, or the imposition of a civil remedy against someone other than the trustee.

The petitioner relies heavily on a lower court New Jersey case, *Plevy* v. *Schaedel*, 44 N. J. Super. 450, 130 A. 2d 910 (Superior Court, Law Division, 1957), and the statutory interpretation of the court in contrasting the legislative treatment given by the State of New Jersey to public improvements as against private improvements.

Respondents contend this reliance is unwarranted for the following reasons:

(1) The *Plevy* case is clearly distinguishable from our case in that *Plevy* involved a suit against officers of the corporate debtor-trustee for a diversion and not one against the statutory trustee for an accounting; (2) The Supreme Court of New Jersey, in its footnote reference to the private improvement statute in the *Hiller & Skogland* v. *Atlantic Creosoting Co. Inc.* case, *supra*, cited the case of *Samuel D. Wasserman Inc.* v. *Klahre, supra*, as allowing civil liability under the statute, but did not cite *Plevy*, the only other decision interpreting the statute and more recent in time than *Wasserman*; (3) In the same footnote reference, the court noted that a different legislator introduced the private improvement statute than the one who introduced the public improvement statute; and (4) A closer look at the public and private improvement statutes demonstrates that the differences in substance are nil, and they were treated differently only because of a different approach by the two legislators introducing the respective bills.

Respondents contend that the statements in the *Hiller & Skogland* and *Wasserman* cases, constitute clearcut support for its view that civil remedies are available under the New Jersey statute. Further statements in the *Hiller*

& Skogland opinion lend strength to this conviction and demonstrate that as between the parties, the beneficiaries must prevail. With respect to the trust fund statute on a public job, which should apply equally to a private improvement, the Supreme Court of New Jersey said:

> "While it cannot be said that the trust fund prescribes a full-blown trust relationship all the way down the ladder with consequent effect upon strangers to the construction project, the underlying thought is clear that all those directly involved should do the right and honorable thing . . ."

and later, the Court said:

> "A court should not hesitate to translate that legislative conception into a positive duty and to compel the appropriate use of payments where the payee knows their source and obviously intended purpose . . . for a court to do less would be to sanction sharp practice—indeed immoral conduct—in the business community. That day should have long since passed as far as the judiciary is concerned."

Its endorsement of the *Wasserman* case, its failure to cite *Plevy* v. *Schaedel,* its mention that different legislators introduced the public improvement and private improvement statutes, coupled with the sweeping language of its decision insofar as the public improvement statute was concerned, make it evident that the Supreme Court of New Jersey would sanction the relief granted by the Court of Appeals.

The court in the *Plevy* case cited two cases in support of its decision, the *Wasserman* case, *supra*, and *Raymond Concrete Pile Co.* v. *Federation Bank & Trust Co.*, 288 N. Y. 452, 45 N. E. 2d 486, affd. on reargument, 290 N. Y. 811, 48 N. E. 2d 709. These cases likewise are distinguishable in that both involved efforts to impose constructive trusts on funds in the hands of third parties not mentioned in the

statute who lacked notice of the trust fund character of the monies. In neither case was relief sought directly against the statutory trustee.

In the *Wasserman* case, a job claimant who had accepted checks from the debtor in release of a mechanic's lien sought to recover monies collected by another creditor on a sheriff's execution against the debtor's bank account. The court refused to impress a trust against the execution creditor on the ground that such action was not authorized by the statute.

However, in rejecting the trust beneficiary's claim, the court nevertheless enunciated principles which support the relief sought herein, to wit, that criminal statutes do have incidental effects and civil remedies arising therefrom. The following are excerpts from the opinion:

> "We are satisfied that had Candrille violated the statute, the plaintiffs would have had whatever *civil remedy might be appropriate to the circumstances under the general principles of law and equity* but Candrille did not violate the statute; the sheriff levied on the fund without leave of Candrille . . .
>
> "The mingling of the fund with other monies in Candrille's general bank account did not destroy plaintiff's *interest in the funds* . . .
>
> "The interest that plaintiff actually had in the account was at most an undisclosed equitable lien . . .
>
> "In New Jersey, there is no clear rule on the subject . . . We think that in each case the facts must be analyzed to determine on broad principles whether the judgment creditor or the lienor has the stronger claim . . ." (Emphasis added.)

A careful reading of the *Wasserman* case indicates (1) that job claimants embraced within the statutory protection have an interest in the fund as trust beneficiaries and (2)

that under certain circumstances, including, but surely not limited to a violation of the statute by the trustee, civil remedies would be available (other than for goods sold and delivered). An accounting by the trustee, either in a bankruptcy, insolvency or estate proceeding, should likewise be available as a logical outgrowth of the *Wasserman* decision.

It should be noted that in neither the *Plevy, Wasserman* nor *Raymond Concrete* cases did the courts sanction a misappropriation of the debtor's trust funds by the debtor itself.

A comparison of the public and private improvements does not lead to any contrary result.

In the early part of 1932, three statutes were passed, dealing with mortgagors, general contractors and sub-contractors respectively on private improvements, and with changes not relevant herein, these laws are in effect today as Sections 2A:102-9, 2A:102-10 and 2A:102-11. Later in 1932, a different legislator introduced two other separate statutes dealing with public improvements, and which are now embodied in Sections 2A:44-148 and 2A:102-12.

Section 2A:102-11, the private improvement statute we are dealing with, provides as follows:

> "All monies received by a subcontractor . . . from a contractor, for the purpose of having a building erected . . . . *are trust funds in the hands of the subcontractor to be applied to the amount of all claims due or to become due and owing from the subcontractor to all persons furnishing . . . materials* to him. . . . Any subcontractor or any officer, director or agent of the subcontractor, who pays or consents to the appropriation of such funds for any other purpose prior to the payment of all claims and charges for the payment of which the funds constitute a trust fund, is guilty of a misdemeanor." (Emphasis added.)

It should be noted that this section consists of two sentences. The first sentence provides that all monies received by a subcontractor are *trust funds* in the hands of the subcontractor *to be applied to the amount of all claims due or to become due to materialmen and others.* The second sentence of the statute creates the criminal offense.

Section 2A:102-12, the public improvement statute, differs from the private improvement statute but these differences favor respondents' view herein. It provides as follows:

> "All monies paid by the state . . . to any person . . . for the making of any public improvement, *shall constitute a trust fund in the hands of such person as contractor.* Any such person who shall use any of the moneys so received for a purpose other than the payment of claims for labor or material . . . is guilty of a misdemeanor." (Emphasis added.)

Thus, this statute is also in two parts, but the first part ends with the establishment of the trust fund in the hands of the contractor and *does not contain any directions about its application nor does it name any beneficiaries.* The second sentence simply creates the criminal offense for misuse of the fund.

Section 2A:44-148, also dealing with public improvements, starts off by repeating substantially the same language as appears in the first part of 2A:102-12 (the criminal statute) but then continues with an application clause, as follows:

> "All monies paid by the State of New Jersey . . . shall constitute a trust fund in the hands of such person as such contractor *until all claims for labor, material . . . shall have been fully paid.*" (Emphasis added.)

It is apparent that the legislator, in the case of the public improvement statutes, wished to separate the civil from the criminal and accomplished that objective by handling the application of the trust funds in a separate statute. In the case of the private improvement statutes, the civil and criminal provisions were handled together and the first sentence of those statutes embodies all the elements of a trust, i.e., a trustee, a fund, directions as to its use and specified beneficiaries.

The public improvement criminal statute (2A:102-12) is obviously only criminal because the clause creating the trust ends without stating its purpose or providing for its application, and logically so, for the disposition of the trust fund is dealt with in 2A:44-148, where the legislator restated the creation of the trust but added the words "until all claims for labor, materials . . . shall have been fully paid". In contrast, substantially the same words were already contained in the private improvement statute, Section 2A:102-11 which provided that "All monies . . . are trust funds in the hands of a subcontractor to be applied to the amount of all claims . . . due . . . from the subcontractor to all persons furnishing . . . materials . . ."

Respondents therefore submit that a closer examination of the New Jersey statutes draws one to the conclusion that no inference can be drawn by any different legislative treatment, except an inference favorable to the respondents, to wit, that both groups of statutes created civil remedies, but in different ways, only because the legislator on the public improvement statute merely desired more clarity and an orderly separation of the civil from the criminal provisions.

If the law of New Jersey is to be determined by a choice between the lower court decision of *Plevy* or the Appellate Division decision of *Wasserman*, it is clear that *Wasserman*, especially in the light of its approval by the Supreme Court of New Jersey in the *Hiller & Skogland* case, is

a more authoritative exposition of New Jersey law than *Plevy*. And the *Wasserman* case clearly keeps the door open for civil remedies under the statute.

In any event, neither the *Wasserman* nor the *Plevy* case is clearcut authority for the factual situation involved herein—a conflict between job claimants on the one hand and the debtor and, indirectly, its unsecured creditors on the other hand. On this conflict, there are no New Jersey cases directly in point. It is submitted, therefore, that the Court of Appeals was free to determine what the highest court of the state would rule in a similar case.

The other case cited in the *Plevy* case, *Raymond Concrete Piling Co.* v. *Federation Bank & Trust Co., supra,* also involved rights of a third party under a comparable New York criminal statute, but the dicta in that case which seemed to deny a civil remedy was later disapproved by the New York Court of Appeals in the case of *Aquilino* v. *U. S. A.*, 10 N. Y. 2d 271, 276, when it said:

> ". . . This holding, distinguished from the dicta in that case, clearly supports the view that a 36-a contractor-trustee holds the funds he receives as trustee, rather than as owner, until he has paid the claims of all the statutory beneficiaries."

There are three cases in the federal courts which are squarely in point, and while they involve application of the law of New York, the statute then involved, Section 36-a of the Lien Law, was similar to the present New Jersey statute, i.e., it was on its face criminal in impact, and yet, the Federal Courts did not hesitate to impress a trust when the fund was in the possession of the bankrupt or debtor. *Albert Pick Co.* v. *Travis*, 6 F. Supp. 486 (E. D. N. Y. 1933); *In re Heintzelman Const. Co.*, 34 F. Supp. 109 (W. D. N. Y. 1940); *Wickes Boiler Co. Inc.* v. *Godfrey-Keeler, Inc.*, 2 Cir., 116 F. 2d 842, mod. 121 F. 2d 415, cert. den. 314 U. S. 686.

Section 36-a of the Lien Law of New York was captioned: *"Contractor who diverts funds guilty of larceny"*.

The Court, in *Albert Pick Co.* v. *Travis, supra,* held that the funds in the hands of the contractor were trust funds under the New York criminal statute and so aptly said:

> "The intention of the Legislature of the State of New York was to protect sub-contractors, materialmen and laborers-contractors cannot avoid their responsibilities by making preferential payments out of trust funds and then filing petitions in bankruptcy or having involuntary petitions filed against them. To follow the trustee's contention that the funds should be distributed among all the creditors would nullify the very purpose of the statute, which was to distribute the specific fund to a preferred class of creditors. There would be no purpose for the lien law were it not that the State intended to protect the very class that the statute outlined. If the contractor attempts to deprive the lienors of their rights, the court should restrain and not help facilitate the avoidance of lawful obligations."

The case of *Wickes Boiler Co., Inc.* v. *Godfrey Keeler, Inc., supra,* is even more authoritative because it involved an application to a Referee in a Chapter XI bankruptcy proceeding for an order similar to the one herein, except that the petitioners there sought to impress a trust on a receivable and not on monies in the debtor's bank account. The *Wickes Boiler* case dealt with the same criminal statute as in the *Albert Pick Co.* v. *Travis* case, and the debtor likewise sought to use the monies to consummate a settlement with its creditors. The Circuit Court of Appeals sustained the Referee in impressing a trust.

Several other related cases support the respondents' view. *Maull* v. *Stokes,* 31 Del. Ch. 188 (1949); *Estate of Liebman,* 189 Misc. 282, 60 N. Y. S. 2d 482; *In Re Korsder's Estate,* 168 Misc. 553, 6 N. Y. S. 2d 324.

In the *Plevy* case, the Court said that since the statute is a criminal one, it should be strictly construed. While this is a general rule of construction, it is also firmly established that where a statute is both remedial and penal, the remedial part will be liberally construed and the penal part strictly construed. Respondents are not attempting to penalize or imprison the debtor; they are only seeking to recover monies which the legislature intended them to receive. See *State* v. *Meinken*, 10 N. J. 348 (1952); *Filardo* v. *Foley Bros. Inc., supra.* Moreover, appellants contend that the statute is so clear that it calls for little or no construction as between the sub-contractor and the materialman.

The remedies cited by the petitioner as being available under the laws of New Jersey dealing with mechanic's liens and "stop notices" are only concerned with tying up monies in the hands of the owner of the real property improvement, whereas the trust fund statutes are designed to insure that monies in the hands of a contractor or sub-contractor are paid over to materialmen and other sub-contractors. And while the Appellate Court in the *Wasserman* case did mention the fact that a lien could have been filed in weighing the equities of the parties, the court there was not dealing with a controversy between the trustee and the beneficiaries, but between the beneficiaries and a third party, nor did the court in the *Wasserman* case hold that filing of a lien or "stop notice" was a condition precedent in order to receive "whatever civil remedy might be appropriate under the circumstances." Cf. *Wickes Boiler Co., Inc.* v. *Godfrey-Keeler, Inc., supra.*

A trust was properly impressed on equitable principles. It is elementary that a Court of bankruptcy is also a Court of equity, and in view of all the facts and circumstances in this matter, the Court of Appeals was correct in affording relief herein on general principles of equity and justice. *Clews* v. *Jamieson*, 182 U. S. 461 (1901); 1 *Pomeroy on Equity Jurisprudence*, Section 158.

The record reveals quite clearly that the petitioner made no excuse for its attempt to prefer a small group of job creditors to the exclusion of and without notice to thirty-five others. The circumstances show that the petitioner was aware of trust fund claims (16a). When its payments to the select few were revealed, it made an about-face and denied any trust fund obligations (17a).

If the petitioner is allowed to use trust funds in this manner, then surely it would be a simple matter for any contractor to misappropriate construction funds with complete immunity by merely receiving all funds on a New Jersey job in the State of New York. The contractor would thereby thwart the New Jersey criminal statute and be free of any trust fund obligations, or the contractor could simply hold the monies in a New Jersey bank account indefinitely, file a Chapter XI petition, with no consequences to it for not paying out to its job creditors.

Surely a Federal Court, under principles of equity, should not permit a debtor to violate the New Jersey statute and frustrate the intent of the New Jersey legislature. Such interpretation of the legislative intent should not be made by any court, no less a court of bankruptcy and equity.

The Court of Appeals also relied on numerous New Jersey cases which hold that where a fund is created for a special purpose even though it does not fall within the confines of the statutory trust, a trust will be impressed under general equity principles. *National Surety Corp.* v. *Barth*, 11 N. J. 506 (1953); *Morris Picker* v. *City of Bayonne, et al.*, 60 N. J. Super. 251; *Wilson* v. *Robert A. Stretch, Inc.*, 44 N. J. Super. 52, 58; *Stulz-Sickles Co.* v. *Fiedburn Const. Corp.*, 114 N. J. Eq. 475.

It would seem immaterial that the foregoing cases involved the public improvement statutes, and the Court of Appeals correctly used all the equitable principles at its command, such as not allowing a person to avoid

responsibility by violating a statute, estoppel, having equity to do what should be done, applying a fund for its intended use when the fund is under the control of a court and other principles of law and justice, in order to grant the relief prayed for herein. See *Filardo* v. *Foley Bros., supra.*

If the petitioner is to prevail in this case, would it not be tantamount to holding that the very ones whom the law was intended to protect were helpless to secure that protection, and, even in New Jersey, that the petitioner would be immune from criminal prosecution so long as it retained possession of the fund indefinitely, or, as in this case, received the funds outside of the State of New Jersey and would be free to divert same in or out of a bankruptcy Court? Respondents do not believe that this Court will countenance such a result, or that the case is the kind of case warranting the exercise of this Court's discretionary review.

Under the strict tests for discretionary review, there must be an actual conflict with applicable local law decisions. See Weiner, 68 Harvard Law Review 20, 61. Such conflict is not present in this case. To the contrary, the decision of the Court of Appeals is in accord with New Jersey law.

CONCLUSION

For the foregoing reasons it is respectfully submitted that this petition for a writ of certiorari should be denied.

Respectfully submitted,

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New York, N. Y. 10005.

SCHWARTZ, WEISSBERGER, LEICHTER & STORCH,
IRVING RONALD STORCH,
Of Counsel.

APPENDIX

UNITED STATES DISTRICT COURT,

EASTERN DISTRICT OF NEW YORK.

No. 62-B-934

In the Matter

—of—

J. E. SCHECTER CORPORATION,

Debtor.

ORDER

The petitioners Carrier Corporation, American Radiator & Standard Sanitary Corporation, Sarco Company, Inc. and Sarcotherm Controls, Inc. having appealed to the United States Circuit Court of Appeals for the Second Circuit from an order of the Hon. Leo J. Rayfiel, one of the Judges of this Court, entered in this proceeding on the 17th day of November, 1964, which denied a petition for review of an order of The Honorable William J. Rudin, Referee in Bankruptcy, dated the 20th day of July, 1964, to the extent that the petition sought to impress a trust on funds in the possession of the debtor, and to recover counsel fees out of said funds, but which granted the petition for review to the extent that the matter was remanded to the Referee for the purpose of directing the debtor to proceed with an appropriate motion to recover funds paid to six creditors pursuant to a prior order of the Referee dated July 23, 1963, and said Circuit Court of Appeals having issued its order dated the 21st day of May, 1965, and its mandate dated the 11th day of June, 1965 having been transmitted to and received by the Clerk of this Court

on the 14th day of June, 1965, wherein it was ordered, adjudged and decreed that such order of the District Court be reversed, with costs assessed at $282.66 in favor of petitioners-appellants, and that the matter be remanded to the District Court for further proceedings in accordance with the opinion of the Court wherein it was held that the District Court erred in not impressing a trust on the funds in question and directed that counsel fees be awarded out of said funds as determined by the District Court, and that the alternative relief of directing the recovery of funds paid to six other creditors was moot.

Now, upon the aforesaid order, mandate and opinion of the United States Circuit Court of Appeals for the Second Circuit, it is

ORDERED, ADJUDGED and DECREED that the sum of $92,316.87 and any additions or accretions thereto paid by William L. Crow Construction Company to the debtor on account of the real property improvement known as "Engineering Quadrangle" at Princeton University, Princeton, New Jersey, pursuant to the order of this Court dated July 23, 1963, constitute and are trust funds in the hands of said debtor to be applied first to the payment of unpaid claims of all persons furnishing labor and materials to J. E. Schecter Corporation for the erection, construction and completion of said improvement or any alteration, repair or addition thereto, and any other reasonable and necessary charges in connection therewith, and it is

FURTHER, ORDERED, ADJUDGED and DECREED that J. E. Schecter Corporation is liable to the petitioner Carrier Corporation, in the sum of $9,029.50 with interest from July 30, 1963, for materials furnished in connection with such improvement, and the said petitioner Carrier Corporation is entitled to share in such trust funds in the

amount and extent as aforesaid and J. E. Schecter Corporation is liable to petitioner American Radiator & Standard Sanitary Corporation in the sum of $2,610.00, with interest from July 30, 1963, for materials furnished in connection with such improvement, and the said petitioner American Radiator & Standard Sanitary Corporation is entitled to share in such trust funds in the amount and extent as aforesaid and J. E. Schecter Corporation is liable to Sarco Company, Inc. in the sum of $363.45 with interest from July 30, 1963, for materials furnished in connection with such improvement, and the said petitioner Sarco Company, Inc. is entitled to share in such trust funds in the amount and extent as aforesaid and J. E. Schecter Corporation is liable to Sarcotherm Controls, Inc. in the sum of $176.64 with interest from July 30, 1963 for materials furnished in connection with such improvement, and the said petitioner Sarcotherm Controls, Inc. is entitled to share in such trust funds in the amount and extent as aforesaid, and it is

FURTHER, ORDERED that all other persons having claims for labor or materials furnished to J. E. Schecter Corporation in connection with the aforesaid improvement, and any other reasonable and necessary charge in connection therewith, be given notice by the attorneys for the petitioners to file verified claims with the attorneys for the petitioners on or before September 15, 1965, and on default to be forever barred from making any claim to said trust fund, said notice to be accompanied by a copy of this order, and it is

FURTHER, ORDERED that the debtor furnish to the attorneys for petitioners a certified list of the unpaid claims against such trust fund, setting forth its best available information of the full name and address of each claimant and the amount of its respective claim, within ten days after service of a copy of this order, and it is

FURTHER, ORDERED that petitioners shall serve said notice to file claims and a copy of this order upon each of said claimants by certified mail, return receipt requested, and it is

FURTHER, ORDERED that the following notice be published once in the Long Island Daily Press, a newspaper published in the County of Queens, State of New York, and once in the Princeton Herald, a newspaper published in Princeton, the County of Mercer, State of New Jersey:

"UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

No. 62-B-934

In the Matter

—of—

J. E. SCHECTER CORPORATION,

Debtor.

To:

All persons who have furnished labor or materials to J. E. Schecter Corporation for the erection, construction and completion of the Engineering Quadrangle at Princeton University, Princeton, New Jersey, or any alteration, repair or addition thereto and any other reasonable and necessary charges in connection therewith.

PLEASE TAKE NOTICE that an order has been entered in the United States District Court for the Eastern District of New York impressing a trust on funds in the possession of J. E. Schecter Corporation, debtor, obtained from William L. Crow Construction Company and arising out of an improvement in the State of New Jersey known as the "Engineering Quadrangle",

Princeton University, Princeton, New Jersey, to be applied to the payment of claims of all persons who have furnished labor or materials to J. E. Schecter Corporation for the erection, construction or completion of said improvement or any alterations, repairs or additions thereto, and any other reasonable or necessary charges in connection therewith, and providing for counsel fees to be paid out of said funds to the attorneys for the petitioners, and

PLEASE TAKE FURTHER NOTICE that you are hereby required to present your verified claim to the office of William J. Rudin, Referee in Bankruptcy, 195 Willis Avenue, Mineola, New York no later than the 15th day of September, 1965, and in default thereof you will be barred from making any claim to said trust fund or any part thereof,

SCHWARTZ, WEISSBERGER & LEICHTER
Attorneys for Petitioners
141 Broadway
New York, N. Y. 10006''

and it is

FURTHER, ORDERED that counsel fees shall be paid to Schwartz, Weissberger & Leichter, attorneys for the petitioners, out of said trust funds in an amount to be determined pursuant to a further order of this Court on application by said attorneys at such time as they deem it appropriate and in conjunction with the order of distribution of the trust funds to the beneficiaries thereof at which time a judgment for costs shall be entered in favor of petitioners in a sum to be taxed by the Clerk of this Court.

Dated: Mineola, N. Y., July 29, 1965.

WILLIAM J. RUDIN,
Referee in Bankruptcy.